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C O N F I D E N T I A L SECTION 01 OF 03 TOKYO 005574

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TAGS: [ECON](#) [ETRD](#) [PREL](#) [EFIN](#) [EAID](#) [JA](#) [IN](#)
SUBJECT: GOJ STRUGGLES TO UPGRADE INDIAN ECONOMIC
RELATIONSHIP

Classified By: Ambassador J. Thomas Schieffer for reasons 1.4 (b/d).

Summary

1. (C) Despite India's position as a top Japanese aid recipient from 2003-05, growth in Japan-India trade over the past five years has lagged behind growth in India's trade with China, the United States, and others. What growth that has occurred has been one-sided, and Japan now ranks below the UAE and Switzerland as an Indian export market. Japanese diplomatic efforts to deepen the relationship, centered on the possible launch of negotiations for a free trade agreement in December, have increased over the past 18 months. The Ministry of Foreign Affairs (MOFA) also reorganized its Southeast and Southwest Asia coverage in August to emphasize India as a strategic partner (and potential counterweight to China). Interministry conflict in Tokyo continues, however, over concrete steps to enhance the partnership. End summary.

MOFA Reorganizes Asia and Aid Bureaus

2. (C) On August 1, the Japanese Ministry of Foreign Affairs (MOFA) created a Southeast and Southwest Asian Affairs Department within the Asian and Oceanian Affairs Bureau, as well as reorganized its official development assistance (ODA) planning functions in a new International Cooperation Bureau (to be reported septel). One of MOFA's goals for the new Asian department is to strengthen ties with India, Southwest Asia Division officials Naoshige Aoshima and Shinsuke Okawa told Econoff in recent meetings.

3. (C) Noting that MOFA's India desk officers increased from three to five, Aoshima pointed out that a new director general (DG) position had also been created. In the previous structure, he explained, the director general for Asian affairs inevitably found himself preoccupied with events in China and North Korea; the new structure would allow for more attention to the rest of Asia from senior officials. (Note: In MOFA's organizational charts, the head of the Southeast and Southwest Asian Affairs Department carries the English title of director general but appears to fall in the hierarchy between the Asian and Oceanian Affairs Bureau DG

and the bureau's Deputy DGs. Aoshima, however, stated the new DG would report directly to MOFA Deputy Ministers Nishida and Yabunaka.)

Despite Aid, Bilateral Trade Growth Lags China's

14. (SBU) India was the largest bilateral recipient of budgeted Japanese ODA in fiscal years 2003, 2004, and 2005. Its package for 2005 consisted of almost 156 billion in yen-denominated loans for infrastructure projects (around \$1.3 billion). These loans, largely tied to procurement from Japanese contractors and vendors, constituted 24.7% of all external assistance received by India and more than 27% of Japan's global yen loan commitments.

15. (SBU) Private-sector companies are present as well, with Japanese foreign direct investment in 2005 increasing by 91.6%, albeit from a relatively small base. Over 300 Japanese companies, including high-profile names like Suzuki, Honda, and Toyota, have a stake in India. Suzuki's initial 1982 investment and joint venture has been highly successful, leading to approximately 50% market share in the Indian domestic passenger car market, according to MOFA, and Toyota's 1997 investment spurred related supply chain companies to follow. (Note: Keidanren contacts informed us that some Japanese multi-nationals have invested in India as a hedge against uncertainties in China's business climate. With that said, Japanese FDI in China, both flow and stock, far outpaces that with India.)

16. (SBU) Despite the large aid commitments and high-profile investments, growth in Japan-India trade has lagged behind growth in India's trade with China, the United States, ASEAN,

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and European competitors. For example, according to MOFA, where Japan-India trade rose from approximately \$3.6 billion in 2000 to approximately \$5 billion in 2004, China-India trade rose from a lower base of approximately \$2.3 billion to over \$12 billion. Over the same time period, U.S.-India trade rose from around \$12.5 billion to approximately \$20 billion.

17. (SBU) Most of the growth in Japan-India trade since 2000 has come in the form of Japanese exports, which rose from around \$1.8 billion to an estimated \$3 billion while Indian exports to Japan have wavered around \$1.8 billion, according to statistics cited by the JSG. Consequently, Japan's share of the Indian external economy has been shrinking. Whereas Japan was India's third largest export market in 1997, it now ranks tenth. MOFA internal briefing papers now show Japan as less important to India as an export market than the UAE, Belgium, Singapore, or Switzerland.

Proposed EPA at Heart of Diplomatic Response

18. (C) Unsurprisingly, India's increasingly vibrant relationships with China and others have caused concern among MOFA officials, Aoshima told Econoff. Noting the sharp increase in bilateral trade between India and the United States, England, Germany, ASEAN, and China, Aoshima stated some have a sense that Japan "missed the boat" in India. He added the GOJ has sharply increased its efforts to strengthen the bilateral relationship since Prime Minister Koizumi paid an official visit to India in April 2005 and signed a joint statement on the "strategic orientation" of the "Japan-India Global Partnership."

19. (SBU) In line with the joint statement's vision of improved relations on multiple fronts, including annual prime ministerial meetings, enhanced security and counter-terrorism dialogs, increased cultural and scientific exchanges, and cooperation in multilateral fora, there have been at least twelve ministerial visits between the countries in the past year. The prime ministers held bilateral talks twice on the margins of other meetings, and a reciprocal official visit to

Japan by Prime Minister Singh is expected in December.

¶10. (SBU) The heart of the expanding agenda, however, is the move toward an "Economic Partnership Agreement" (EPA), in essence a free trade agreement. In preparation for the reciprocal summit, the India-Japan Joint Study Group (JSG) released a report in June 2006 recommending negotiations toward an EPA. The JSG, which was founded after the April 2005 summit, was co-chaired by Japan's Deputy Minister of Foreign Affairs Mitoji Yabunaka and Ashok Jha, Yabunaka's counterpart in India's Ministry of Finance.

¶11. (C) MOFA's hope is that Prime Minister Singh will agree to launch EPA negotiations during a December visit, according to Aoshima, who stated that a detailed agreement would take at least two years of negotiations. Aoshima, who took part in the JSG's work, noted that the most difficult issues for the two sides were already clear. Japan's desire for lowered tariffs would be difficult for Indian industrial interests, and India will likely press for access for agricultural goods and to Japan's labor market for engineers and other skilled workers. Aoshima, who called his Indian counterparts "tough negotiators," speculated that Japan's recent inclusion of provisions for Philippine nurses and caregivers in its EPA will only make the labor issues thornier.

GOJ Agencies Have Mixed Priorities on India

¶12. (C) Tough Indian negotiators will not be the only challenge MOFA faces as it tries to realign policy, programs, and development assistance to bring new emphasis to India as a regional partner. In preliminary discussions about expanding Japan's presence through a new consulate in Bangalore, Japanese Ministry of Finance representatives reportedly told MOFA that a new consulate would be fine -- as long as MOFA identified which other one it wanted to scrap.

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Similarly, Ministry of Economy, Trade, and Industry enthusiasm for an Indian EPA, when floated in the media, drew the immediate ire of the ministries responsible for agricultural and labor affairs. While our contacts have stated that incoming Prime Minister Abe sees India as a strategic counterweight to China, they also lament that no routine interministerial process exists to iron out agency differences over how to transform the bilateral relationship.

Comment

¶13. (C) MOFA's reorganization will bring more working level and senior ministry attention to Japan's relationship with India, but the interministerial conflicts already evident will require higher-level intervention to further efforts toward upgrading the relationship.

SCHIEFFER